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The growth of the multinational hotel industry: 1946 to the 1960s.

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Introduction

Historically, compared to research on the internationalisation of the service sector, such as the areas of banking, auditing, communication and management consultancy, only limited studies have been undertaken on the hotel sector. One reason why so little has been written about hotel internationalisation is that there are significant problems relating to the definition of the word ‘hotel’ both as a term and a sector. The hotel business shares the same capital-intensive nature as the manufacturing industry, but the latter was able to measure productivity easily through the tangible products it produced. In the case of the hotel, although the capital-intensive nature of hotels lies in a considerable investment in fixed assets such as buildings, land and extensive furnishings, fittings and equipment (Guilding, 2009), hotel operations can be more complex than the tangible image portrayed. The intangible nature of the hotel industry complicates performance and growth measurement. Broadly, a hotel provides services such as food, beverages and accommodation and is a form of business.

Traditionally, a large hotel has had to coordinate the provision of a range of hospitality services, in addition to rooms, including the sales of food and beverages, laundry and other retailing business within the hotel premises (Guilding, 2009). In addition, the hotel business depends on the simultaneous consumption and production nature of rendering hotel services (Clancy, 1998; Enderwick, 1989); and the heterogeneous nature of the interactions between providers and guests make it difficult to provide an accurate measurement of productivity or comparable business performance.

Although the historical development of current international hotel chains - Intercontinental Hotel Group, Hilton Hotel Corporation (HHC), Marriott International Inc., Starwood Hotels & Resorts and their portfolio developments such as Intercontinental Hotels, Hilton International, JW Marriott Hotels & Resorts and Sheraton Hotels respectively – has been discussed in trade journals and books, an in-depth analysis of the reasons driving such a frenzy of internationalisation of hotel chains after the Second World War (WWII) have been less explored. The question addressed in this paper is: What drove hotel companies to expand overseas after WWII? This paper employs two case studies of the two pioneering hotel chains that lead the internationalisation process after WWII to examine the drivers of such process: the Intercontinental Hotel Corporation (IHC) and the Hilton Hotel International (HHI). Archival documents and secondary data were collected to conduct this study. The next section reviews the drivers of multinational hotel growth with reference to IHC and HHI. The final section presents the conclusion for this paper.

The Drivers of Multinational Hotel Growth

The growth of multinational hotel companies emerged after WWII, driven mainly by the US-based hotel companies. The main determinants found driving such growth were US foreign policy, and the growth of the airline and related tourist industries. In the late 1940s, many countries in different regions were recovering from the aftermath of WWII. Two regions possessed the opportunity for business development and were attractive to the US government: Latin America and Europe. It was believed that tourists and their expenditure was the ‘only source of revenue that could possibly be harvested in amounts large enough to be of immediate aid’ to these economies (Friedlander, 1949: 66). The US government deployed foreign aid to reach out to these regions to help them recover from WWII damages, in turn, creating trading markets for itself.

The US Government was interested in the Latin American hotel projects for reasons including the promotion of travel between the two continents to solidify their relationships; facilitating business travel and penetrating the Latin-American market; and injecting US dollars into the Central and South American nations via a policy of increasing the number of American tourists to these countries (New York Times, 1947a). Juan T. Trippe (Trippe), CEO of Pan America World Airlines (Pan Am) was assigned by the (then) US President Franklin Roosevelt (President Roosevelt) to survey the situation in Latin America and it was found that a shortage of decent accommodation discouraged business and tourist travel into those regions (Pan American, 1961). At the time, however, there were no US companies willing to participate in establishing hotels in Latin America, and President Roosevelt asked Trippe to develop 5,000 hotel rooms in some 20 countries south of the US

border (Potter, 1996). Trippe formed IHC in 1946, as a subsidiary of Pan Am, with the intention of developing these hotels. In addition to receiving financial support from Pan Am, IHC also obtained some financial support from the Export-Import Bank, with the help of the government. The Export-Import Bank was created under the Reconstruction Finance Corporation (RFC) to finance US export sales (Potter, 1996). The agreement allowed each hotel owning company designated by Pan Am a maximum loan amount of \$25,000,000 on the condition of a 20-year repayment period and a two-year moratorium from its first draw-down of funds (Pan American, 1945). The Export-Import Bank also limited the loan to 50% of the cost of equipment, materials, supplies and services in the respective hotels. In addition, the hotels had to pay interest at the rate of 4% per annum on outstanding balances. Furthermore, either the Government of the country within which the hotel was to be constructed or an accredited banking institution had to guarantee unconditionally the repayment of advances against any line of credit established between the Export-Import Bank and the hotel units concerned.

Similarly, HHC started its internationalisation process after WWII, driven by US foreign policy. In 1947, Conrad Hilton was approached by the US government to explore the possibility of creating a chain of Hilton Hotels in Europe as part of the Marshall Plan programme (Maximaxims, 1951). The Marshall Plan set the goals of generating \$2 and \$2.5 billion through tourist receipts from Americans travelling to Europe between 1950 and 1954 (Friedlander, 1949). The Economic Cooperation Administration (ECA), created by the Marshall Plan, was to oversee the economic and technical assistance programmes extended to help a few selected European countries to re-generate their economies. These

programmes included an ECA fund allocated for European hotel development, contributed by the US State Department, which required a repayment rate of 2% below market rate (HHI, 1952; Pearson, 1949).

Agreeing with the US government's views on using tourism to generate economic growth, foreign governments helped to boost the tourism industry by eliminating extensive paperwork for tourist visa applications. A number of European countries abolished visa requirements for short-term travellers from the US by late 1948 (Friedlander, 1949). Similarly, many countries in the Caribbean eliminated visa requirements after 1949, especially for US citizens, to facilitate the movements of tourists between national borders (New York Times, 1954). On the other hand, unlike most European and Caribbean countries, the majority of South American governments required tourists to carry visas, except for Mexico, which required a tourist card and passport (Szulo, 1954). The restrictions implemented by South American governments could have been one reason among many that slowed down international tourist growth, and had an impact on the differences between IHC's and HHI's financial performance (to be discussed later in this section).

Presented with the pull from business opportunities arising in Europe due to the need to repair buildings in anticipation of the arrival of American tourists (Friedlander, 1949) and the push exerted by US foreign policy, Conrad Hilton created HHI to expand overseas. HHI was established as a subsidiary of HHC with the original funding of \$500,000 and was expected to depend on further sources of finance to develop its international hotel

programme. Despite being invited to develop a hotel chain in Europe under ECA funding, HHI did not subsequently develop any hotels through this fund. The reasons were a lack of cooperation from the ECA people in Europe and the end of the Marshall Plan in 1951 in conjunction with the Vietnam War (1950 – 1953) resulting in the withdrawal of funds made available for hotel developers (HHI, 1952). Between 1949 and 1966, HHI operated 24 hotels (see Table 1). HHI's first international hotel was built in Spain in 1953 and subsequent hotels were established in Latin America, North America (Canada), the Caribbean, and Middle East regions. In the same period, IHC established 35 hotels (see Table 1). The chain concentrated on Latin America and the Caribbean islands between 1949 and 1956, and only established its first IHC hotel outside those regions, in the Middle East region, in 1961 (Potter, 1996). Europe in the early 1950s was not a prioritised region for expansion of IHC, as most European capitals were deemed to be densely operated by existing small and medium-sized hotels (Potter, 1996).

The boom in the airline industry, driven by airline technology advancement and related tourism growth, was another determinant for facilitating multinational hotel growth. From the 1940s, technology in the airline industry advanced exponentially, contributing to shorter flight times. For instance, it took six days to fly between San Francisco (USA) and Manila (Philippines) in 1935, but it only took an overnight journey to fly across the Pacific in 1960 (PAWAIAR, 1960). The US deregulation that allowed more foreign-flag airlines to increase their operations between the US and world destinations after WWII intensified the competition between US airlines and reduced their revenue and earnings (Barnum, 1998). At the same time, it was difficult for US airlines to compete with other unregulated state-

owned foreign-flag airlines, which obtained financial support from their governments and were unrestrained over their pricing and routes (Button, 1998; New York Times, 1959; PAWASAR, 1945).

Following the intensified competition, the costs of air tickets became more affordable particularly with the introduction of tourist class tickets. Pan Am was the first airline company to launch tourist class tickets in September 1948, operating between New York and San Juan, priced at \$75, for a one-way ticket, which was 30% cheaper than the usual first class ticket (PAWASAR, 1948; PAWAIAR, 1952; 1953). This move was followed by Trans World Airlines (TWA) in October 1948 and other airlines (Pan American, 1954) which further hastened the rate of change in international tourism development.

Complementing the airline technology and pricing change was the combination of economic and socio-cultural changes. After WWII, US companies became leaders in their industries and the US dollar emerged as the world's major reserve currency (Jones, 2005) driving the increased demand for international tourism among the American middle class. In 1950, 12 million families in the US had disposable income after taxes of at least \$4,000 and this figure rose to an estimated 36 million in 1960 (Pan American, 1956). Consumer expenditure on foreign travel by US residents also rose between 1947 and 1959. For example, the dollar amount spent by American travellers increased from \$688 million in 1947 to \$853 million in 1948, and \$1.61 billion in 1959 (Friedlander, 1949; New York Times, 1947b). The percentage of US overseas journeys via air also rose exponentially between 1950 and 1955. For instance, 31.4% of American passengers travelled by air in

1950, and this figure increased to 70% by 1955 (PAWAIAR, 1951; 1955). As a result of international tourism growth, a greater demand for hotel rooms arose worldwide.

The foreign government policy and airline industry no doubt were important drivers of multinational hotel growth. Factors internal to the individual companies also played some influential role in facilitating such growth. This will be reviewed in the light of IHC's and HHI's financial performances. Despite entering the international hotel market at about the same time, the financial performances of IHC and HHI showed striking differences between 1949 and 1964¹ (see Table 2). HHI was making profits throughout its overseas operations while IHC only made a profit for the first time in 1954, and incurred quite significant losses throughout the period under discussion. Three reasons are considered for such asymmetric performance in the companies' internationalisation processes: the hotel locations, the business models and the management experience.

Firstly, IHC's first few hotels were located in Latin America, a region that incurred a financial loss between 1950 and 1953, mainly as a result of numerous episodes of political unrest and economic problems. During the periods of unrest, IHC was operating, constructing or negotiating in Chile, Columbia, Uruguay, Venezuela, Brazil, Argentina, Peru, Ecuador, Guatemala and Mexico (Matthews, 1952; Pan American, 1948; Pan American, 1951). Although IHC's profit saw some improvement after 1954 due to a major re-organisation of the company, the financial situation continued to be affected by external

¹ This comparison stops at 1964 because HHI was spun off in 1964. Moreover, with the advent of the jet age, more US hotel chains have developed outside of the American continent and increased competition in the international hotel industry by then.

political problems. For example, in December 1958, Fidel Castro took over Cuba and the political unrest deterred people from visiting the country. Subsequently, American-owned or -operated businesses were expropriated, including those of IHC and HHI (Phillips, 1960). HHI also incurred its first financial loss in 1958 caused by the political unrest in Cuba; however, the overall loss for HHI was smaller compared to the loss suffered by IHC. It is apparent that HHI's diversified geographical presence enabled the company to reduce investment risk derived from the political unrest which IHC was facing.

IHC's initial choices of hotel location in Latin America were prescribed in response to the government foreign policy. In 1959, with the advent of the jet age, Pan America was concerned that its new jet aeroplanes might be flying empty seats to areas of the world that did not have decent accommodation to attract visitors. Consequently, IHC's locations were identified and proposed by Pan Am's regional divisions (Atlantic, Latin America and Pacific) (Pan American, 1959). In contrast to IHC's internationalisation venture which started with strong intentions for a noble venture, HHI's motivation was grounded on business opportunity and profitability from the start (HHI, 1948), which explained in part the reasons for such disparity in financial performance. Conrad Hilton believed that the business opportunities available in Europe were beneficial for HHC's growth and persuaded his Board of Directors to expand into the region despite their reluctance to commit because of their worries about 'war', 'revolution' and 'inflation' (Hilton, 1957: 234).

Secondly, the business models adopted by IHC and HHI did not only account for the differences in financial performance between the two companies; they also played a critical role in providing insight into the drivers of international hotel growth. IHC's business model for international mode of entry started as management contracts because of regulations imposed in countries that the company expanded into (Potter, 1996). For instance, it was believed that 'the civil code of most Latin American countries, which was based on the laws of Napoleon, gave special rights of tenancy to lessee: thus it could be difficult to expand into this region via the leasing method' (Potter, 1996: 20). Although management contracts enabled a company to expand with a minimum equity investment, IHC did not make use of this advantage. Instead, the company invested substantial equity in each of its ventures, due to the decision made by Pan Am to take part of the equity in order to show other shareholders and investors IHC's confidence in their own management.

In contrast to IHC, HHI's financial commitment was limited to the provision of operating capital, and local government or private companies invested in individual hotel properties. One of the reasons was due to HHI holding a well established reputation as a hotel operator. The other reason was ascribed to HHI's founder, Conrad Hilton's management approach. Although Conrad Hilton was enthusiastic about hotel internationalisation, he was cautious not to commit huge capital investments and risk. HHI's robust financial performance stemmed from its clearly set out lease model which the company held onto for many years. The model was based on a '2/3 and 1/3' lease contract, meaning the hotel owner(s) received two thirds of generated profit, and HHI received one third (HHI, 1959). This method was adopted after HHI's first expansion beyond the North American continent

- the Caribe Hilton Puerto Rico, which successfully generated \$102,963 in net profit in the first year of operation (1949 -1950) (HHI, 1960) and continued to show positive returns in subsequent years (see Table 2).

Generally, leasing incurs higher costs than management contracts as the nature of the latter lies in minimum equity investment and only involves working capital for daily operations (Uttam, 1984). Although the lease model employed by HHI was able to sustain a constant growth for its international expansion, the loss incurred by its Cuban venture eventually steered HHI towards the management contracting mode, in recognition of the benefits to expansion without committing high capital cost, as well as enabling the company to retain its operations and reputation. Ultimately, this entry mode entailing low capital risk played a driving role in incentivising hotel companies to expand overseas.

Thirdly, management experience was the other major cause of the profitability difference between HHI and IHC. The nature of their original business and management teams played an important role in this instance. HHI originated from a US domestic hotel company and was led by Conrad Hilton, whose 27 years of hotel operation experience, combined with his centrally controlled operating style, became an advantage for HHI during the internationalisation process. HHI also formed a special Operating Committee, comprising three senior executives and headed by Conrad Hilton, to make important decisions about its development (HHI, 1947). Conrad Hilton was also the President of both HHC and HHI, which enabled important decisions to be made quickly regarding HHI's development.

In contrast to HHI's board of directors which was selected from a pool of management with prior hotel operating experience, IHC was conceived by a US international airline company. The management team of IHC's operations was overseen by directors who held responsibilities on both Pan Am and IHC boards. However, Pan Am did bring in Lucius Boomer (Boomer), the only experienced hotel operator, to start and grow IHC. Boomer did not have full control of IHC expansion. The fact that most of the directors of IHC were airline personnel and not hoteliers enabled Pan Am to play a major role in deciding IHC's locations and business partner-seeking process. Therefore, it is argued that the location selections, business models adopted, and management experience reflected to some extent the determinants or deterrents which drove or delayed the international hotel growth.

Conclusion

In conclusion, the determinants found for the growth of multinational hotel chains was initiated by the foreign policies, stemming from the fact that the US government wanted to build a good relationship with its neighbour, Latin America, and extend its trade aid to war-torn European countries at the end of WWII; and the pull by host governments had the effect in part of growing tourism and the hotel internationalisation process. Moreover, the timing of a shortage of foreign currency amongst these countries, specifically of US dollars, and the need for US dollars to facilitate imports, presented the US government with the opportunity to improve its international social and economic relationship with them, and form a symbiotic relationship. In conjunction with governments' motivation, the rise of the wealth of the American economy and the increase in the middle-income population further stimulated demand for travel. These economic and social changes coincided with the

improvements in airline technology, and the emergence of shorter flight time and cheaper air tickets. The interaction of these events resulted in international tourism growth and drove the need for countries to provide quality accommodation in order to meet the demand capacity and attract visitors.

One major cause of financial loss in the hotel internationalisation process was its high dependence on political and economic conditions. This cause illuminates the high risks and difficult decisions hotel companies must face in order to become multinational. The physical hotel product makes it difficult for hotel companies to quickly adapt purpose-built rooms to suit changes in political climate and market demand. In addition, their simultaneous production and consumption feature by definition requires hotels to be physically present in several locations to generate business, compelling hotel operators to take risks despite the knowledge of political risks which could lead to expropriation and decline in demand. This study presents the analysis of the determinants of hotel multinational growth, filling the void in the limited literature on their multinational growth. Not dissimilar to other service sector studies, this paper illuminates the roles of governments and the motivation of hotel multinationals in following another industry, specifically the airline sector, into the international domain.

Table 1: HHI's & IHC's International hotels development, 1949 - 1964

HHI			IHC		
	Hotel name	City/ Country		Hotel name	City/ Country
			1949	Grande Hotel	Belem/Brazil
			1950	Carrera Hotel	Santiago/Chile
			1950	El Prado Intercontinental	Barranquilla/Colombia
			1952	Reform Intercontinental	Mexico City/Mexico
1953	Castallana Hilton	Madrid/Spain	1953	Victoria Plaza	Montevideo/Uruguay
			1953	Princess hotel	Hamilton/Bermuda
			1953	Tequedama Intercontinental	Bogota/Colombia
			1953	De Lago Intercontinental	Maracaibo/Venezuela
			1953	Tamanaco Intercontinental	Caracas/Venezuela
1955	Istanbul Hilton	Istanbul/Turkey			
1956	The Continental Hilton	Mexico City/Mexico	1956	Nacional de Cuba	Havana/Cuba
1957	El Panama Hilton	Panama City, Panama	1957	Jaragua Intercontinental	Santo Domingo/Dominican Republic
			1957	Embajador Intercontinental	Santo Domingo/Dominican Republic
			1957	Curacao Intercontinental	Curacao/Netherlands Antilles
			1957	Varadero Oasis	Varadero Beach/Cuba
1958	Queen Elizabeth	Montreal/Canada	1958	El Salvador Intercontinental	San Salvador/El Salvador
1958	The Berlin Hilton	West Berlin/Germany	1958	El San Juan Intercontinental	San Juan/Puerto Rico
1958	Habana Hilton	Havana/Cuba			
1959	Nile Hilton	Cairo/Egypt			
1959	Las Brisas Hilton	Las Britsas/Mexico			
1960	The Virgin Isle, Hilton	St Thomas/ US Virgin Islands	1960	El Ponce Intercontinental	Ponce/Puerto Rico
1960	Royal Hilton	Teheran/Iran			
			1961	Phoenicia Intercontinental	Beirut/Lebanon

HHI			IHC		
	Hotel name	City/ Country		Hotel name	City/ Country
1962	Hilton International Trinidad	Port of Spain/Trinidad	1962	Ducor Intercontinental	Monrovia/Liberia
1962	Amsterdam Hilton	Amsterdam/Netherlands	1962	Hotel Indonesia	Jakarta/Indonesia
			1962	Southern Cross Intercontinental	Melbourne/Australia
1963	Hilton International London	London/UK	1963	Dublin Intercontinental	Dublin/Ireland
1963	Athens Hilton	Athens/Greece	1963	Cork Intercontinental	Cork/Ireland
1963	Hilton International Rotterdam	Rotterdam/Netherlands	1963	Limerick Intercontinental	Limerick/Ireland
1963	Cavalieri Hilton International	Rome/Italy	1963	Frankfurt Intercontinental	Frankfurt/Germany
1963	Hong Kong Hilton	Hong Kong	1963	Ivoire Intercontinental	Abidjan/Ivory Coast
1963	Tokyo Hilton	Tokyo/Japan	1963	Singapura Intercontinental	Singapore/Singapore
1963	Dorado Hilton	Dorado, Puerto Rico	1963	Mandarin Hotel	Hong Kong
1963	Jamaica Hilton	Ocho Rios/Jamaica			
1963	Montreal Aeroport Hilton International	Montreal/Canada			
1964	Hotel Vancouver	Vancouver/Canada	1964	Intercontinental Jordan	Amman/Jordan
1964	Hilton International Mayaguez	Mayaguez/Puerto Rico	1964	Intercontinental Wien	Vienna/Austria
			1964	Intercontinental Geneva	Geneva/Switzerland
			1964	Intercontinental Jerusalem	Jerusalem/Israel
			1964	Karachi Inter-continental	Karachi/Pakistan
			1964	Okura Hotel	Tokyo/Japan
			1964	Esplanade Intercontinental	Zagreb/Yugoslavia

Source: HHCAR various years; HHI (1965); PAWAIAR & PAWASAR various years; Potter (1996).

Table 2: HHI's & IHC's net profit (US\$), 1950-1964

	HHI	IHC
1950	102,963	-305,000
1951	243,855	-229,000
1952	295,368	-347,000
1953	386,351	-340,000
1954	489,952	235,000
1955	688,315	286,000
1956	909,922	497,000
1957	992,468	301,000
1958	637,512	-345,000
1959	935,898	-478,000
1960	1,260,012	-246,000
1961	1,151,572	111,000
1962	1,266,000	-245, 000
1963	1,503,000	-345, 000
1964	1,449,000	491,000

Source: HHCAR (1961); HHIAR (1964); HHI (1965); HHI (1967); Pan American (1971).

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